No. 2428

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

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ANDREW CLAUSS, VICTOR ENGINGER, W. A. GRUBB, JOSEPH HAMM, K. HALTER, L. SCHOTT, L. LAIT, E. W. CLARK, JEAN A. GOURSELLE, M. C. BROOKE, H. L. BROOKE, JESSE W. OLNEY, LILLY M. STEWART, THEODORE B. WILCOX, F. L. SHULL and ALVIN J. WHITMAN,

Appellants,

vs.

PALMER UNION OIL COMPANY (a corporation), FRANK L. BROWN, LEWIS A. HILBORN, GEORGE L. WALKER, CHARLES E. LADD, GAVIN MCNAB, H. C. STRATTON, and GEORGE I. STEWART, as directors of said Palmer Union Oil Company (a corporation), and in their respective and individual capacities, FRANK L. BROWN, J. C. KEMP VAN EE, LEWIS A. HILBORN, H. C. STRATTON and CHARLES E. LADD, as directors of Palmer Oil Company (a corporation), and in their respective and individual capacities, ANGLO-CALIFORNIA TRUST COMPANY (a corporation), and PALMER OIL COMPANY (a corporation),

Appellees.

BRIEF FOR APPELLEES.

GAVIN McNAB,
B. M. AIKINS,
R. P. HENSHALL,
ROBERT R. MOODY,
NAT SCHMULOWITZ,
Solicitors for Appellees.
LUTHER ELKINS,
Solicitor for Appellees, George I. Stewart and Gavin McNab.
GAVIN McNAB,
Solicitor for Appellee, Anglo-California Trust Company.

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Appellees.

BRIEF FOR APPELLEES.

Statement of the Case.

This is an appeal from a final decree dismissing a suit brought by Andrew Clauss against the Pal-

mer Union Oil Company, the directors of that company, and other parties. The suit was brought by Clauss, claiming to be a stockholder of the Palmer Union Oil Company, and the relief sought by the original bill of complaint was, in part, as follows: It sought to recover back from the Palmer Union Oil Company the physical assets which it alleged had been transferred by the Palmer Oil Company to the Palmer Union Oil Company; and it prayed an injunction, pending the determination of this question, restraining the collection of an assessment upon the capital stock of the Palmer Union Oil Company. The original bill is not in the record. The amended bill, upon which the decree appealed from was entered, further seeks relief by way of accounting, and also seeks to recover from the directors of the Palmer Union Oil Company, the value of the property transferred, as well as the consideration for such transfer from the transferee. To this bill, a motion to dismiss on the part of all the defendants, some of them appearing separately, was made. These motions were granted, and in accordance with the Court's order, a final decree dismissing the bill was entered.

A somewhat detailed statement of the proceedings in the Court below is necessary to understand the points arising on this appeal.

The original bill was filed on October 7, 1913 (p. 93), and on October 8th (id.), the Court entered

an order to show cause why a temporary restraining order should not issue pending the suit, returnable on October 11th. The purpose of this order to show cause was to secure a temporary injunction restraining the collection of the assessment just referred to upon the capital stock of the Palmer Union Oil Company. In response to this order to show cause, it was pointed out that the main object of the bill was to set aside the transfer *of property* from the Palmer Oil Company to the Palmer Union Oil Company, made in consideration of an issue of stock, and that in consequence, the plaintiff could have no standing to complain of an assessment upon the stock of the Palmer Union Oil Company *if he won the suit.* In other words, only upon the theory that plaintiff lost his case, could he be entitled to an injunction. Accordingly, the order to show cause was denied (p. id.).

On November 7, 1913 (p. 94), before any of the defendants had defended in the case, Victor Enginger and fourteen other persons claiming to be stockholders of the Palmer Union Oil Company, filed petitions to intervene, and their interventions were granted (p. 94). The great majority of these interveners were citizens of the State of California (see p. 80), and the Court could have no jurisdiction over their bills, *which are identical with the plaintiff's bill,* as original bills. The petitions to intervene and the bills in intervention are not found in the record.

On November 8, 1913 (p. 4), the defendants, some of them appearing separately, filed motions to dismiss the bill. On the 15th of November, 1913, before any of these motions had been heard, the plaintiff obtained leave to file an amended bill (id.), and such an amended bill was filed, which is found in the record (pp. 1 et seq.).

On November 25, 1913 (p. 94), in response to the service of this amended bill, the defendants, some of them appearing separately, filed their several motions to dismiss the bill. On January 19, 1914, *the clerk* entered an order taking the amended bill *pro confesso* as to all the defendants (see p. 58). This order was entered notwithstanding the fact that defendants had filed their motions to dismiss the amended bill as required by the rules (see pp. 43 et seq.), and before any hearing or determination on this motion had been had.

On January 24, 1914 (pp. 60 et seq.), the defendants, separately appearing, filed an application to vacate and set aside the order purporting to take the amended bill *pro confesso*. The principal ground of this motion was that they had appeared in response to the service of the amended bill by motion to dismiss. The application was heard on January 26, 1914, and was promptly granted (p. 69). On January 29, 1914, the motions to dismiss, themselves, came on for hearing before the Court, and were argued and submitted. On March 2, 1914 (p. 71), the Court granted these motions

to dismiss, pursuant to an opinion which is found in the record (p. 69). On March 4, 1914 (p. 72), a final decree dismissing the bill in accordance with the opinion of the Court, was entered.

On March 10, 1914 (p. 73), after the record had been enrolled, the plaintiff filed a motion to amend the order granting the motion to dismiss, and seeking to vacate the final decree entered pursuant thereto (p. 73). On April 3, 1914 (p. 81), this motion was denied in an opinion, which is likewise found in the record (p. 79).

See,

Clauss v. Palmer Union Oil Co., 213 Fed. 286.

It will thus be seen that this cause was heard on four separate occasions in the Court below. First, on an application for a temporary injunction pending the action; secondly, on an application to vacate a *pro confesso* order upon the ground that the parties were not in default; thirdly, on a motion to dismiss the bill; and, fourthly, on a motion to vacate and set aside the decree dismissing the bill.

Other facts necessary to an understanding of the case, including a statement of the substance of the bill, will be stated as we proceed with the argument.

Brief for Appellees.

I.

THE ORDER VACATING THE ORDER PRO CONFESSO ENTERED BY THE CLERK WAS PROPERLY MADE, AS (A) THE ORDER PRO CONFESSO ITSELF WAS VOID, FOR NONE OF THE PARTIES WAS IN DEFAULT, AND IN ANY EVENT, THE ORDER RESTED IN (B) THE DISCRETION OF THE LOWER COURT,—AND THE EXERCISE OF SUCH DISCRETION WILL NOT BE INTERFERED WITH ON APPEAL.

The first point urged by the appellants is that the Court's order vacating the order *pro confesso* against the Palmer Union Oil Company, Lewis A. Hilborn and Palmer Oil Company, was error. The answer is, that neither of the parties was in default at the time the order *pro confesso* was entered; and in any view, the discretion exercised by a trial Court in opening a default will not be interfered with on appeal.

Preliminarily, it should be noted that the plaintiff caused the default of *all the defendants,* as well as of the three defendants referred to, to be entered. He entered the default of Frank L. Brown, George L. Walker, Charles E. Ladd, Gavin McNab, H. C. Stratton and George I. Stewart, individually and as directors of the Palmer Union Oil Company, including Lewis A. Hilborn as a director of that company, and Frank L. Brown, J. C. Kemp Van Ee, Lewis A. Hilborn, H. C. Stratton and Charles E. Ladd, as directors of the Palmer Oil Company, and in their individual capacities, the Anglo-California Trust Company and the Palmer Oil Com-

pany (p. 59). It is now conceded that the default was improperly entered as to all of the defendants, except the three named.

1. The action of the Court below was clearly right. Not one of the defendants was in default, and the order *pro confesso* was void. The facts are these:

The defendants, other than Palmer Union Oil Company and Lewis A. Hilborn, within the time required by the equity rules, filed their motion to dismiss the original bill (p. 94). The Palmer Union Oil Company and Lewis A. Hilborn answered (p. 93). This was in accord with Eq. Rule 29, which requires that defenses heretofore set up by demurrer, be set up by answer or by motion to dismiss.

The plaintiff, then, by leave of Court, filed an amended bill (p. 94).

Under Rule 32, it became obligatory upon all the defendants to answer this amended bill within ten days, unless the time was enlarged by the Court. Within ten days after the service of the amended bill, all the defendants appeared and filed their motions to dismiss the amended bill (pp. 43 et seq.). They were not, therefore, in default.

The appellants urge a strange and highly technical contention in this regard. They assert that as Rule 32 provides, "In every case where an amendment to the bill shall be made after answer filed, the defendant shall put in a new or supple-

mental answer within ten days," the defendants Hilborn and the Palmer Union Oil Company were precluded from filing a motion to dismiss the amended bill. Indeed, it was contended in the Court below, that where an amended bill was filed, no right to move to dismiss it existed on the part of any defendant. But this position seems now to be abandoned. But it is now contended that where a party has answered an original bill, he is precluded from moving to dismiss an amended bill. This construction of the rule, we think, leads to a manifest absurdity.

Rule 29 provides "that every defense, in point of law, arising upon the face of the bill" must be taken either by motion to dismiss or in the answer.

Upon the filing of an amended bill, therefore, it is plain that a defendant would have the right to take advantage of every defense which arises upon the face of the bill by either a motion to dismiss or answer. If the fact that a defendant has answered an original bill shall preclude him from moving to dismiss an amended bill, it is quite easy to deprive a defendant of his right to move to dismiss an action and to compel him to answer in every case. For by filing a bill of complaint, to which the defendant would either voluntarily answer, or, upon his motion to dismiss being denied, be compelled to answer, and thereupon amending the bill in more important particulars after answer filed, the complainant would successfully preclude

a defendant from moving to dismiss this amended bill; he would thereby compel an answer to a cause of action interjected into the case for the first time after answer filed. This construction of the rules works a manifest hardship upon the parties, and would, in effect, lead to the denial of the right to move to dismiss a defective amended bill.

Moreover, the default claimed would not prove to be of any value to the plaintiff in this case. The Court could enter no decree as to the defaulting defendants, upon a bill which it orders dismissed. See *Snow v. De La Vega,* 15 Wall. 562. Being a stockholders' suit, and the relief running against the corporation, its officers and directors, no effective decree could be entered unless all parties were in default, and the defense of one would enure to the benefit of all.

Snow v. De La Vega, 15 Wall. 562.

2. The default as to Palmer Oil Company was void upon its face. It never at any time appeared in the suit. The service of process attempted to be made upon the Palmer Oil Company was void. It affirmatively appears from the marshal's return (p. 41) that he served it upon a person who was *not* the secretary of the company, and that at the time the company had no legal existence (pp. 41, 42). The bill of complaint alleges that prior to the commencement of the suit, the Palmer Oil Company went out of existence (p. 25). The pro-

posed amendment to the bill recognizes that this company had no legal existence (p. 77). There being no corporation known as the Palmer Oil Company at the time the suit was commenced, the service of process upon it was utterly void (see *Newhall v. Western Zinc Mining Co.,* 164 Cal. 380); and the fact that the service of process was void appears upon the face of the return and upon the face of the bill itself. There was no one who could appear in the name of the Palmer Oil Company, and no one appeared for it. It would have been, indeed, a misdemeanor, under the laws of California, for which any officer of the corporation, or for any attorney of the company to have attempted to appear for it; by so doing he would have made himself criminally liable under Sec. 9 of the Act of March 20, 1905, as amended (see *Newhall v. Western Zinc Mining Co.,* supra).

3. It will, of course, be conceded that an order vacating a default decree will rarely, if ever, be set aside in an appellate court. The disposition, of course, is to hear matters upon their merits, and where a *nisi prius* tribunal has exercised its discretion in favor of such a trial, such discretion will never be reviewed in an appellate tribunal.

In the present case, however, there was no final decree *pro confesso,* as referred to in Rule 17. That rule provides that when an appeal is taken *pro confesso,* the Court may proceed to a final decree at any time after the expiration of thirty

days after the entry of the order *pro confesso;* and it further provides that such a final decree *pro confesso* shall be deemed absolute, unless the Court shall, at the same term, set aside the same, or enlarge the time for filing the answer. Here it is contemplated, inferentially at least, that final decrees *pro confesso* may be set aside, with the proviso, however, that no such motion shall be granted except upon payment of costs, and unless the defendant shall undertake to file his answer, as directed by the Court, for the purpose of speeding the cause. The order *pro confesso* in the case at bar was not a final decree *pro confesso,* but was the preliminary order *pro confesso,* which is grantable, of course, by the clerk, under Rule 5, and that rule says that all orders grantable by the clerk,—among which, of course, is the decree taking bills *pro confesso,*—"may be suspended or altered or rescinded by the judge upon special cause shown." The application in the Court below was an application to the judge, under this rule, to rescind the order *pro confesso* entered by the clerk. As the cause had not proceeded to a final decree, and could not at that time have resulted in a final decree until the expiration of thirty days from the order *pro confesso,* a ruling by the judge, in the exercise of his discretion, vacating the order *pro confesso* by the clerk, is hardly reviewable in this Court.

And no decree of any kind could be entered on this alleged default, as the cause was at issue with respect to other defendants.

See

Snow v. De La Vega, supra.

4. Finally, the plaintiff himself admitted that his bill was defective and must be amended. Such an amendment would open the default as to all. Hence appellants' first point is, in reality, a moot one.

II.

THE AMENDED BILL IS MULTIFARIOUS, AND IS CLEARLY SUBJECT TO THE OBJECTION THAT IT OMITS THE JOINDER OF NECESSARY PARTIES.

1. One of the grounds for dismissing the suit in the Court below was, that the Palmer Senior Oil Company, and the bondholders of the Palmer Union Oil Company, were necessary parties to the suit (p. 70). It is very clear that this objection is well taken.

The amended bill shows that the Palmer Senior Oil Company was incorporated under the laws of the State of California (p. 10), and that thereafter, in consideration of the capital stock issued to the individual defendants by that corporation, they transferred to it an option to purchase a certain tract in the Santa Maria Oil fields; that thereafter the Palmer Senior Oil Company transferred to the Palmer Union Oil Company all of the assets of said

corporation, including said option, to the Palmer Union Oil Company; and that the consideration paid said Palmer Senior Oil Company by said Palmer Union Oil Company for said option and assets was the capital stock of said Palmer Union Oil Company, amounting to 1,750,000 shares of said Palmer Union Oil Company.

It further appears from the amended bill that a bonded debt was created by the Palmer Union Oil Company upon all of its property, including the property transferred to it by the Palmer Oil Company (p. 29). The defendant Anglo-California Trust Company is alleged to be the trustee of this bonded debt. The complaint further alleges that the Palmer Union Oil Company has sold $500,000 of these bonds to various persons (p. 30), and that $250,000 of them were deposited with the defendant Anglo-California Trust Company as security for the $250,000 which was to be paid by the Palmer Senior Oil Company for the property under the option aforesaid (p. 30).

All these transactions are alleged in the bill to have been fraudulently done, and relief against them is sought in this suit. The character of this relief is indicated by the fifth prayer of the amended bill, which reads as follows (p. 36):

> "5. That the transaction whereby said Union Company acquired from said Palmer Senior Oil Company the said option to purchase of defendant Anglo-California Trust Company the lands covered by said option, in security for the purchase of which lands by

> said Union Company two hundred thousand dollars of bonds of said Union Company were by said Union Company deposited with said Anglo-California Trust Company, be rescinded in so far as said bonds constitute any lien or claims upon the assets of said Palmer Company, and that all mortgages or other liens or claims upon the property of said Palmer Company, so transferred to said Union Company, executed, made or given by said Union Company, be declared null and void and of no effect.''

It is very clear, from the foregoing statement, that the relief sought by the bill, or any relief warranted by this statement of facts, cannot be awarded without the presence of the Palmer Senior Oil Company. That company is not alone a proper and necessary party, but is, indeed, an indispensable party. How can the transfer from the Palmer Senior Oil Company to the Palmer Union Oil Company of certain property be undone and cancelled, as is sought by this amended bill, without the presence of the Palmer Senior Oil Company? How can any kind of relief be awarded to plaintiff in this action without considering the rights of the Palmer Senior Oil Company, and giving it an opportunity to be heard? This appears to us to be so plain as to require no further discussion.

2. The bondholders of the Palmer Union Oil Company are likewise clearly necessary parties to this suit, and the objection taken below on this ground is well taken. The statement of the contents of the bill under subdivision 1, supra, is suffi-

cient to show the merits of this objection. Recapitulating that statement, it appears from the bill that after all the property of the Palmer Senior Oil Company, together with the physical assets of the Paula, the Palmer Junior and the Palmer Oil Company, had been transferred to the Palmer Union Oil Company, that company created a bonded indebtedness upon its property. This bonded indebtedness constituted a first lien upon its assets. The bill then alleges that the Palmer Union Oil Company "sold $500,000 of said bonds, and the money derived therefrom, the amount of which is unknown to your orator, said directors recklessly and wantonly spent partially upon said property and partially for purposes unknown to your orator" (p. 30). The bill further alleges, as already stated, that $250,000 of these bonds were deposited with the defendant Anglo-California Trust Company as security for the payment of the $250,000, the purchase price agreed to be paid for the option on the real property aforesaid. We have already quoted paragraph 5 of the prayer of the bill, from which it appears that the lien of this mortgage upon the assets of the Palmer Union Oil Company is sought to be cancelled and annulled, as well as a cancellation of the transaction whereby the Palmer Union acquired the option and other property from the Palmer Senior Oil Company.

It appears, therefore, that a large number of bonds are outstanding in the hands of third persons. The holders of these bonds suppose that they have

a first lien upon the property of the Palmer Union, which includes all the assets of the Palmer Oil Company, Palmer Senior, Palmer Junior and Paula Oil Companies. In this action, there is sought a judgment cancelling this lien. Obviously, it is not necessary to cite authority to the point that the kind of relief prayed for, or any relief warranted under the facts stated in the bill in this connection, cannot be granted until these bondholders are made parties defendant and given an opportunity to be heard. This point likewise appears so plain to us that we forbear to discuss it, and the ruling of the Court below in this connection was clearly correct.

In this regard, it is contended by appellants that this objection was not made in the Court below. But it was not necessary for appellees specifically to make this objection. The bondholders were indispensable parties, and the Court below knew that it could not award any relief consistent with the case made, without their presence. While, as a general rule, it is true that the objection that parties are not joined as defendants is deemed waived unless specifically made, there are instances in which the Court, of its own motion, is in duty bound to make this objection.

See

O'Connor v. Irvine, 74 Cal. 435;
Winter v. McMillan, 87 Cal. 265;
Mitau v. Roddan, 149 Cal. 1.

This doctrine is especially true in the Federal Court, where the jurisdiction of the Court being

special and limited, though general in its character within its proper sphere, the relief awarded must be complete in itself.

See

Carrau v. O'Calligan, 125 Fed. 657.

III.

THERE IS A CLEAR MISJOINDER OF CAUSES OF ACTION IN THE AMENDED BILL, IN THAT (A) IT SEEKS TO SET ASIDE A TRANSFER OF PHYSICAL ASSETS FROM THE PALMER OIL COMPANY TO THE PALMER UNION OIL COMPANY; (B) IT SEEKS TO RECOVER FROM THE DIRECTORS THE VALUE OF THE PROPERTY THUS TRANSFERRED; AND (C) IT SEEKS TO RECOVER FROM THE TRANSFEREE, THE PALMER UNION OIL COMPANY, THE CONSIDERATION FOR SUCH TRANSFER.

It is very plain that these causes of action cannot properly be joined in the same suit. The first one, for example, involves a rescission of the transaction complained of; the others involve an affirmance of its validity. Causes of action which are antagonistic, and indeed, mutually destructive to each other, cannot, of course, be joined in the same complaint. The fact that the amended bill improperly joins these several causes of action, is very easily shown.

As the appellants concede that they attempt to set forth a cause of action for the recovery back from the Palmer Union Oil Company of the assets transferred from the Palmer Oil Company to the

Palmer Union Oil Company, it is not necessary to point out in the amended bill where the facts in support of this alleged cause of action are attempted to be set forth.

It is very easy, however, to show that this bill likewise sets forth facts leading to a recovery from the directors of the value of the property transferred.

Thus, in Paragraph 13 (p. 29), after alleging that the moneys derived from the sale of $500,000 worth of bonds have been recklessly and wantonly spent upon the property, a discovery is prayed with respect to the sundry sums of money, the amounts of which have been paid on account of the purchase of the lands (p. 30). In the succeeding paragraph (p. 31) are found allegations with respect to the extravagant and reckless manner in which the Palmer Union Company is being operated, and discovery is prayed for all the debts, bonds, etc., which may become a charge upon the property of the Palmer Union Oil Company. The bill further sets forth in detail the facts with respect to the consideration which passed from the Palmer Union Oil Company to the Palmer Oil Company for its transfer of the property, and alleges that the subsequent act of the Palmer Union Oil Company in exchanging a portion of this consideration for other property was wrongful and fraudulent, and that it had no right to cancel the bonds which it received as consideration for such transfer (p. 22).

Paragraph 4 of the prayer of the amended bill prays for relief grounded upon these facts, and it reads as follows (p. 36):

> "4. That said Union Company be decreed to restore to all and several the stockholders of said Palmer Company who may join herein and who shall return to said Union Company its said preferred and common stock, their several shares of Palmer Company stock theretofore by them delivered to said Union Company."

Here there is sought, of course, to be recovered from the Palmer Union Company, the transferee, the consideration which was parted with by the Palmer Oil Company for the transfer of its property. In this aspect of the case, of course, the transfer of the assets from one company to the other is affirmed, but the consideration for this transfer is sought to be recovered.

The bill likewise sets forth a third cause of action to recover from the directors the value of the property thus transferred.

Thus, the facts previously set forth, coupled with the allegations as to the value of the property transferred, to wit, that the assets of the Palmer Oil Company were worth $2,500,000 (p. 5), together with further allegations showing the alleged manipulation of the stocks and bonds of the company, state an attempted cause of action for the recovery from the directors, who were guilty of this manipulation, and who were charged as conspirators, of the value of the property thus transferred. Ac-

cordingly, we find that the 7th paragraph of the prayer of the amended bill reads as follows (p. 37):

> "7. That a decree be entered adjudging that the said Frank L. Brown, Lewis A. Hilborn, J. C. Kemp Van Ee, H. C. Stratton and Charles E. Ladd, directors of said Palmer Oil Company at the time said assets of said Palmer Company were transferred to said Union Company and at the time said bonds were delivered to said Union Company, jointly and severally as individuals, pay unto the said Palmer Oil Company for the use and benefit of its said stockholders the sum of two million dollars."

It is too plain, we think, for discussion, that these causes of action cannot be joined in the same complaint, and the ruling of the Court below, therefore, sustaining this objection is clearly correct.

IV.

THE ORDER REFUSING LEAVE TO AMEND WAS CORRECTLY MADE.

1. The decree appealed from is a mere decree of dismissal. It does not dismiss the bill for want of equity, but directs simply that the amended bill of complaint be dismissed (p. 72). The decree, therefore, is not a dismissal on the merits, but a dismissal for the reason stated in the order (p. 71), and does not preclude, and was not intended to preclude, the bringing of another suit, if such a suit lies in the proper forum.

The objection, therefore, urged by appellants' counsel that the decree is one on the merits, and may possibly serve as an estoppel, is not well taken.

2. After the entry of this decree the plaintiff made a motion (p. 73) to amend the order entered March 2, 1914, granting the motion to dismiss, and to vacate and set aside the decree, and for an order granting leave to amend again the amended bill of complaint. This motion sought three kinds of relief, and it will be convenient to consider them separately.

It was sought first to amend the order entered prior to the decree, sustaining the motion to dismiss (p. 75). This order, of course, could not be amended by the Court until the decree dismissing the suit had itself been vacated. The only ground set forth in their motion for amending this order which was made by the Court, is that it was entered without notice to the plaintiff (p. 75), and that no opportunity was given to plaintiff to amend his bill of complaint in accordance with the Court's opinion, and that the Clerk of the Court never mailed or otherwise sent to the plaintiff or his attorneys a notice of the entry of said order. All these reasons are immaterial.

The motion to dismiss was regularly argued and submitted to the Court, and *both* parties were heard. The Court was not bound to notify any party that it was about to render a decision in the case; nor was the Clerk of the Court required to notify counsel that this order had been made. The rule of

Court requiring the Clerk to send copies of orders to the respective parties does not apply to orders made after notice, but only to orders made in the absence of parties who have had no notice of the application (see Eq. Rule 4).

The foregoing remarks apply also to the reasons urged for setting aside the decree. In other words, no reason whatever was assigned why the order directing a dismissal of the bill, and why the decree entered pursuant to that order, should be vacated and set aside.

We come now to the motion for leave to amend the complaint, which, of course, could not be granted until the decree itself was vacated, and which may be regarded as a motion to vacate the decree for the purpose of permitting an amended bill of complaint to be filed. The motion in this particular reads as follows (p. 76 et seq.):

> "That plaintiff above named further moves this Honorable Court that he may be at liberty to amend his said Amended Bill of Complaint in the following particulars:
>
> First: That said Amended Bill of Complaint be dismissed without prejudice, as to the following defendants, viz: Anglo-California Trust Company, a corporation; Frank L. Brown, J. C. Kemp Van Ee, Lewis A. Hilborn, George L. Walker, Charles E. Ladd, H. C. Stratton, Gavin McNab and George L. Stewart, as individuals and as directors either of said Palmer Union Oil Company or as directors of said Palmer Oil Company.
>
> Second: That there be stricken from the first prayer of said Amended Bill of Complaint,

the last line thereof which reads as follows: 'or to a receiver, if such receiver be appointed as hereinafter prayed'.

Third: That the prayers for relief contained in said Amended Bill of Complaint numbered 3, 5, 6 and 7 be stricken out.

Fourth: That so much of said Amended Bill of Complaint beginning with the words 'California, having its principal place of business at Sisquoc', etc., at line 30, page 1, of said Amended Bill of Complaint, and ending with the word 'capacities', at line 14, on page 2 of said Amended Bill, be stricken out, and that there be inserted in lieu thereof the following: 'California, having its principal place of business in the City and County of San Francisco, State of California, and Frank L. Brown, J. C. Kemp Van Ee, Lewis A. Hilborn, H. C. Stratton and Charles E. Ladd, in so far as they claim to be, or may be found to be, Trustees of said Palmer Oil Company, the said Frank L. Brown, J. C. Kemp Van Ee, Lewis A. Hilborn, H. C. Stratton and Charles E. Ladd, claiming that said Palmer Oil Company has been dissolved and no longer exists as a corporation. Complainant alleges on information and belief that there are no creditors existing of said Palmer Oil Company.'

Fifth: That the title of this cause in said Amended Bill of Complaint be amended to read as follows:

Andrew Clauss,

Plaintiff,

vs.

Palmer Union Oil Company, a corporation, Frank L. Brown, Lewis A. Hilborn, George L. Walker, Charles E. Ladd, Gavin McNab, H. C. Stratton and George I. Stewart, as Directors of said Palmer Union Oil Company and in their

> respective and individual capacities, Frank L. Brown, J. C. Kemp Van Ee, Lewis A. Hilborn, H. C. Stratton and Charles E. Ladd, as Directors of Palmer Oil Company, a corporation, and in their respective individual capacities, Anglo-California Trust Company, a corporation, First Doe, Second Doe, Third Doe, Fourth Doe, Fifth Doe, Sixth Doe, Seventh Doe, Eighth Doe, Ninth Doe, Tenth Doe, Palmer Oil Company, a corporation,
>
> Defendants.
>
> Sixth: And complainant prays for such further and other relief as to the Court may seem meet and equitable."

(a) In the Court below, one of the reasons assigned for denying this application was, that the amendment proposed referred only to the prayer of the complaint, and did not in any wise change the amended bill (p. 80).

It will be seen that in thus ruling, the lower Court was correct.

The structure of the bill, with all its objectionable features, remains precisely the same after this amendment is allowed as before. The Court below, therefore, knew in advance, that if it allowed this amendment, *it would be compelled to grant another motion to dismiss.* To justify the Court in vacating a final decree, and to permit the filing of an amended pleading, the pleading proposed must at least be free from the objections found to exist in the previous pleadings. *The proposed pleading here*

is subject to all the objections previously sustained by the Court.

(b) There are other objections, however, to this amendment. It sought to amend the bill of complaint by dismissing, without prejudice, the case as to certain defendants. This was its first amendment (p. 76). This amendment, however, is contradictory of the 5th amendment, in which the title was changed so as to include all the defendants against whom the first amendment proposed that the bill should be dismissed (p. 77).

The second and third amendments sought to strike out a portion of the first prayer of the complaint, and all of the third, fifth, sixth and seventh prayers. The prayers in the complaint, of course, are not important, except as illustrations of the character of the action, and if the facts contained in the bill warranted a particular kind of relief, the Court would be justified in awarding it, even though no specific prayer for that relief were contained in the bill.

The objections urged to the bill were urged as against its substance or structure. These objections are by no means obviated by simply striking from the bill the relief which was prayed, based upon the facts thus stated. *Indeed, it leaves the bill in a more objectionable form than ever.*

The fourth amendment suggested consisted in striking out a certain portion of the narrative part

of the bill, and inserting in lieu thereof, the following (p. 77):

> "California, having its principal place of business in the City and County of San Francisco, State of California, and Frank L. Brown, J. C. Kemp Van Ee, Lewis A. Hilborn, H. C. Stratton and Charles E. Ladd, *in so far as they claim to be, or may be, found to be,* Trustees, of said Palmer Oil Company, the said Frank L. Brown, J. C. Kemp Van Ee, Lewis A. Hilborn, H. C. Stratton and Charles E. Ladd, claiming that said Palmer Oil Company has been dissolved and no longer exists as a corporation. Complainant alleges on information and belief that there are no creditors existing of said Palmer Oil Company."

The effect of this amendment is to leave the bill in a defective form in another particular. By the first amendment, as we have seen, the Anglo-California Trust Company, and *all the directors of the Palmer Union Oil Company,* and the same persons as individuals, were sought to be dismissed from the case (see p. 76). The bill, then, with this last amendment, will run against the Palmer Union Oil Company, the Palmer Oil Company, which it is alleged is disincorporated, and which, under the California decisions, cannot be sued, and certain persons claiming to be directors of the Palmer Oil Company, who are made conditional defendants contingent upon the status fixed upon them by the decree. *They cannot know that they are defendants in fact until after the case is decided.*

But the directors of the Palmer Union Oil Company, however, are necessary parties to this action,

and the allowance of the proposed amendments leaves the amended bill more defective than before.

It is, of course, settled law that in a stockholders' suit, where the directors are charged with fraud, they must be joined as defendants.

Ribon v. Chicago &c. L. Co., 16 Wall. 446;
Wickersham v. Crittenden, 93 Cal. 17;
Woodroof v. Howes, 88 Cal. 184;
Slattens v. St. Louis &c. T. Co., 91 Mo. 217;

See

Hawes v. City of Oakland, 104 U. S. 450.

(c) This leads us to state another reason why the motion to amend was properly denied. The lower Court had ruled that there was a misjoinder of causes of action and a non-joinder of parties. Had an application to amend the bill been made before the decree was entered, such an application should propose an amended bill *at least free from these objections. The amended bill as proposed is subject to the same objections as the original bill. It still misjoins causes of action and makes no offer of any kind to cure this objection. It does not join as defendants the bondholders whom the Court found to be necessary parties to the suit.*

It is decided, and it is plain the decision is correct, that the bondholders are necessary parties to the action. But there is nothing to show that their citizenship is not such as to divest the Court of jurisdiction. The presumption being against the jurisdiction of the Federal Court, this Court cannot

presume that if these bondholders were joined, that their citizenship would be of such a character as to confer jurisdiction upon the Federal Court. Jurisdiction by diversity of citizenship must be made affirmatively to appear. We are led, therefore, to the result that the Court is asked to allow an amendment, and to require the joinder of parties, whose presence the Court does not know will not oust it of jurisdiction. Indeed, we would be justified in saying, under the decisions, that there is a presumption against the jurisdiction of a Federal Court, that until the specific diversity of citizenship has been made to appear, the Court *does* know the citizenship of the parties to be such as to divest it of jurisdiction.

V.

THE MOTION TO AMEND THE COMPLAINT WAS PROPERLY DENIED AND THE SUIT ITSELF WAS PROPERLY DISMISSED, FOR THE REASON THAT IT AFFIRMATIVELY APPEARED ON THE FACE OF THE RECORD THAT THE SUIT DID NOT REALLY AND SUBSTANTIALLY INVOLVE A CONTROVERSY PROPERLY WITHIN THE JURISDICTION OF THE DISTRICT COURT, AND AS PROVIDED IN SECTION 5 OF THE ACT OF MARCH 3, 1875, THAT COURT WAS REQUIRED IMPERATIVELY TO PROCEED NO FURTHER IN THE CASE, EXCEPT TO DISMISS IT.

The record as printed in this case does not disclose, as it should, all the proceedings in the Court below (see p. 93). In denying the motion to amend

the complaint after the decree rendered, the Judge of the Court below said (p. 79):

> "After the filing of said bill, a petition was presented by the attorneys for plaintiff on behalf of fifteen other stockholders of said Palmer Oil Company asking leave to intervene, and such leave having been granted by the Court, said attorneys filed a bill of intervention by said fifteen stockholders identical in all essential particulars with the original complaint. In this bill of intervention twelve of the plaintiffs owning 125,567 shares are citizens of California, and three owning 3,500 shares are citizens of other States. So that if the present motion were granted, we would have a situation with four plaintiffs citizens of other States owning in all 4,500 shares, and twelve plaintiffs citizens of California owning 125,567 shares, all in this court clinging to the complaint of a single stockholder, resident of Ohio, owning but 1,000 shares; and all represented by the attorneys of the original plaintiff. Under these circumstances, aside from the fact that the proposed amendments are for the most part amendments to the prayer of the original bill, and not amendments to the bill itself, the motion to amend will be denied, and it is so ordered."

The omitted portions of the record show this statement of the Judge of the lower Court to be correct. The entire record, if before this Court, will disclose other facts. The bill itself was verified by one of the attorneys for the complainant, Andrew Clauss, and not by the complainant himself (p. 39). This attorney is one of the interveners and is a citizen and resident of California. He is designated as Jesse Olney, solicitor for com-

plainant, and Jesse W. Olney, as intervener. *The same attorneys who appear for the complainant appear as attorneys for the interveners.* While the title of the case in the Court below, up to and including the entry of the final decree, as well as the entry of the order denying the motion to amend the complaint, is, *Andrew Clauss v. Palmer Union Oil Company et al.,* the record shows a joinder of all these citizens in California with the plaintiff in the prosecution of these appeals. Thus, the petition for the allowance of an appeal addressed to the Court below recites that (p. 83):

> "The above named complainant, *and* Victor Enginger, W. A. Grubb, Joseph Hamm, K. Halter, L. Schott, L. Lait, E. W. Clark, Jean A. Gourselle, M. C. Brooke, H. L. Brooke, Jesse W. Olney, Lilly M. Stewart, Theodore B. Wilcox, F. L. Shull, and Alvin J. Whitman, *co-plaintiffs* and interveners in the above entitled cause, conceiving themselves aggrieved"
> * * *

In the assignment of errors, the same language is repeated (p. 85). The order allowing the appeal (p. 88), and the bond (p. 89), run in favor of the plaintiff and the co-plaintiffs. The citation on appeal (p. 100) is in favor of Andrew Clauss and all the other parties as appellants. The order enlarging the time for filing the record on appeal is made in favor of appellants (p. 103), and the title of the case in this Court is not "Andrew Clauss, Appellant, v. Palmer Union Oil Company", but "Andrew Clauss, *and* Victor Enginger, W. A. Grubb, Joseph Hamm, K. Halter, L. Schott, L.

Lait, E. W. Clark, Jean A. Gourselle, M. C. Brooke, H. L. Brooke, Jesse W. Olney, Lilly M. Stewart, Theodore B. Wilcox, F. L. Shull and Alvin J. Whitman, Appellants".

It stands out, therefore, plainly apparent upon the face of the record that this suit was collusively brought by a non-resident stockholder of the Palmer Oil Company in the Federal Court in order to permit the great body of stockholders, who could not themselves go into the Federal Court, to intervene and prosecute this action for their benefit. The suit is simply a convenient means of permitting California stockholders of a California corporation to invoke the aid of a Federal Court in their behalf, where otherwise they could not do so. This being so plainly apparent upon the face of the record, it was the duty of the lower Court to have dismissed the suit upon that ground alone.

If, however, the Court ought not to refuse to entertain jurisdiction, where the bill originally did not disclose that in the background were other stockholders represented by the same attorneys, who were subsequently to intervene, the fact that the action was being prosecuted on behalf of persons who could not get into the Federal Court was certainly a reason for refusing to permit the filing of an amended bill after decree entered, especially where the bill proposed to be filed was defective in substance.

Finally, it is quite clear that the suit was properly disallowed, for the reason that the amended

bill and the proposed amended bill failed to comply with Equity Rule 27, which reads as follows:

> "Every bill brought by one or more stockholders in a corporation against the corporation and other parties, founded on rights which may properly be asserted by the corporation, must be verified by oath, and must contain an allegation that the plaintiff was a shareholder at the time of the transaction of which he complains, or that his share had devolved on him since by operation of law, and that the suit is not a collusive one to confer on a court of the United States jurisdiction of a case of which it would not otherwise have cognizance. It must also set forth with particularity the efforts of the plaintiff to secure such action as he desires on the part of the managing directors or trustees, and, if necessary, of the shareholders, and the causes of his failure to obtain such action, or the reasons for not making such effort."

This rule is mandatory, and the construction which the Supreme Court of the United States has placed upon it is very clearly set forth in *City of Quincy v. Steel,* 120 U. S. 241. This case also sets forth very clearly in its review of the previous decisions of the Court, the circumstances and conditions under which a stockholder may bring suit against a corporation to enforce the rights which the corporation fails to assert. *It also illustrates the application of the Act of March 3, 1875.* We take the liberty of quoting somewhat extensively from this case on all three points, as follows:

> "Prior to 1875 cases had come into the courts of the United States, especially into the circuit courts, where citizenship had been simulated,

and parties improperly made or joined either as plaintiffs or defendants, for the purpose of creating a case cognizable in the circuit courts originally, or removable thereto from the state courts; and as it very frequently occurred that both plaintiffs and defendants were willing to seek that court in preference to the state courts, it had been found very difficult to prevent these improper cases from being tried in those courts. In the Act of March 3, 1875, an attempt was made to correct this evil, and by the fifth section of that Act it was declared 'That if, in any suit commenced in the circuit court, or removed from a state court to a Circuit Court of the United States, it shall appear to the satisfaction of said circuit court, at any time after such suit has been brought or removed thereto, that such suit does not really and substantially involve a dispute or controversy properly within the jurisdiction of said circuit court, or that the parties to said suit have been improperly or collusively made or joined, either as plaintiffs or defendants, for the purpose of creating a case cognizable or removable under this Act, the said circuit court shall proceed no further therein, but shall dismiss the suit or remand it to the court from whence it was removed, as justice may require.'

In the cases of Hawes v. Oakland, 104 U. S. 456 (26:830), and Huntington v. Palmer, Id. 482 (26:833), the question of the growth of the form of invoking federal jurisdiction, where it does not otherwise exist, by the attempt of a corporation which cannot sue in the federal court to bring its grievance into that court by a suit in the name of one of its stockholders who has the requisite citizenship, was very much considered. In order to give effect to the principles there laid down this Court at that term adopted Rule 94 of the Rules of Practice

for Courts of Equity of the United States, which is as follows:

'Every bill brought by one or more stockholders in a corporation, against the corporation and other parties, founded on rights which may properly be asserted by the corporation, must be verified by oath, and must contain an allegation that the plaintiff was a shareholder at the time of the transaction of which he complains, or that his share had devolved on him since, by operation of law, and that the suit is not a collusive one to confer on a court of the United States jurisdiction of a case of which it would not otherwise have cognizance. It must also set forth with particularity the efforts of the plaintiff to secure such action as he desires on the part of the managing directors or trustees, and, if necessary, of the shareholders, and the causes of his failure to obtain such action.'

The bill in the present case, although verified by oath, is far from complying with the letter or the spirit of this rule. It does not contain an allegation that the plaintiff was a shareholder at the time of the transaction of which he complains, although the allegation on that subject includes a part of the time in which the City of Quincy failed to pay for its gas; but inasmuch as the sworn allegation in the bill was made on the 18th day of August, 1885, and he there swears that he had been the owner of the stock on which he brings this suit over four years, it is easy to suppose that he acquired this stock after the 11th day of May, 1881, on which day the City by its official action notified the gas company that it repudiated the contract and would no longer be bound by it. And it is not an unreasonable supposition that the gas company, foreseeing litigation which it might be desirable for that company to have carried on in a federal court, im-

mediately after receiving notice of that resolution had this stock placed in the hands of Mr. Steel for the purpose of securing that object, and though the suit was delayed for two or three years, it was probably because the City continued to pay some part of the demand for the gas furnished by the company. The bill does not contain the allegation expressly prescribed by this rule, that 'The suit is not a collusive one to confer on a court of the United States jurisdiction of a case of which it would not otherwise have cognizance'. The allegation of the bill, 'That this suit is brought in good faith, and for the collection of and to compel the collection of what your orator believes to be a meritorious claim', is by no means the equivalent of this provision of the rule; for it may very well be understood that the party who is seeking to enforce a debt which he believes to be due is acting in good faith for the purpose of compelling its collection, while he may be well aware that he is imposing upon the court to which he actually resorts a jurisdiction which does not belong to it.

The rule also requires that he must set forth with particularity his efforts to secure action on the part of the managing directors or trustees of the corporation of which he is a member, and, if necessary, of the shareholders, and the causes of his failure to obtain such action. In the case before us he seems to have made but a single effort to induce the directors of the gas company to institute a suit against the City to recover the money, and this was by a communication in writing addressed to the board August 1, 1885. No copy of that letter is produced, but it is said that the board of directors laid the communication on the table. No copy of the order of the board upon that subject is produced; no effort at conversation with any of the directors, or any earnest effort of any

kind upon his part to induce the directors to bring the suit is shown in the bill; no attempt to call the attention of the shareholders to this matter during the four years in which he said he was a shareholder, and during which time the City was failing to pay its debt to the gas company, nor any effort at any of the meetings of the shareholders or of the directors to induce them to enforce the rights of the company against the City, is shown. The most meager description possible of a bare demand in writing, made sixteen days before the institution of this suit, is all we have of the efforts which he should have made to induce this corporation to assert its rights. This letter was addressed to the board of directors August 1, 1885, from what point is not stated, but it may reasonably be inferred that it was from Alabama, of which state he was a citizen. The bill itself is sworn to the 13th day of August thereafter. How long a time was left for the consideration of this question by the board of directors, and what earnest efforts Mr. Steel may have made to induce their favorable action, may be easily inferred from the speed with which the bill was sworn to in Alabama and filed after he addressed his letter to the board. The inference that the whole of this proceeding was a preconcerted and simulated arrangement to foist upon the Circuit Court of the United States jurisdiction in a case which did not fairly belong to it, is very strong.

In the case of Hawes v. Oakland, 104 U. S. 461 (26:832), in speaking of this perfunctory effort to induce the trustees of the corporation to act, it is said: 'He (the plaintiff) must make an earnest, not a simulated, effort with the managing body of the corporation to induce remedial action on their part, and this must be made apparent to the court. If time permits or has permitted, he must show, if he fails

with the directors, that he has made an honest effort to obtain action by the stockholders, as a body, in the matter of which he complains. And he must show a case, if this is not done, where it could not be done, or it was not reasonable to require it.' Again it is said: 'He merely avers that he requested the president and directors to desist from furnishing water free of expense to the City, except in case of fire or other great necessity, and that they declined to do as he requested. No correspondence on the subject is given. No reason for declining. * * * No attempt to consult the other shareholders to ascertain their opinions or obtain their action. But within five days after his application to the directors this bill is filed.'

In the case of Huntington v. Palmer, 104 U. S. 483 (26:834), the court says: 'Although the company is the party injured by the taxation complained of, which must be paid out of its treasury, if paid at all, the suit is not brought in its name, but in that of one of its stockholders. Of course, as we have attempted to show in the case just mentioned (Hawes v. Oakland, supra, 450), this cannot be done without there has been an honest and earnest effort by the plaintiff to induce the corporation to take the necessary steps to obtain relief.' See Detroit v. Dean, 106 U. S. 537 (27:300).

We think upon the face of the bill in this case there is an entire absence of any compliance with the rule of practice laid down for equity courts in such cases, and of any evidence of an earnest and honest effort on the part of the complainant to induce the directors of the gas company to assert the rights of that corporation. On the contrary, the clear impression left on reading the bill is that it is an attempt to have a plain common-law action tried in the court of equity, and the rights of

parties decided in a court of the United States who have no right to litigate in such a court, and that there is no sufficient reason in the bare fact that Mr. Steel is a stockholder in the corporation which justifies such a proceeding."

For the reasons stated, therefore, it is respectfully submitted that the conclusion of the Court below is correct, and that the decree appealed from should be affirmed.

Dated, San Francisco,
November 9, 1914.

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